

REQUEST LETTER 07-009

NAME

ADDRESS

Ms Pamela Hendrickson
State Tax Commission
210 North 1950 West
Salt Lake City UT 84134

Dear Ms Hendrickson:

I am a tax researcher employed by COMPANY, a DIVISION. Our unit of COMPANY develops tax compliance software which we market to providers in the telecommunications industry. We are now seeking to expand the contents of our database by accounting for the taxability treatment of a product offering known as “dark fiber”.

In order to determine whether we should code this product offering as either “taxable” or “non-taxable” in your state, I shall now present a hypothetical fact pattern to illustrate the issues we are dealing with followed by a specific set of questions we need answers to.

FACT PATTERN:

XYZ Company is a Local Exchange Carrier licensed to do business in your state. XYZ owns a network of “fiber optic cable: which (when activated) is used to support voice, data, and Internet service applications. The bundles of fiber optic cable are buried underground and accessible only through highly secured “locked-box” locations. XYZ leases the right to use part of this fiber optic cable network to a variety of corporate clients including other providers of telecommunications service. The lease agreements which XYZ enters into with its’ customers limit the rights of those customers exclusively to usage of the fiber optic network, i.e., XYZ maintains ownership of the fiber optic cable infrastructure at all times.

However, what XYZ is leasing is the raw fiber optic cable “capacity”, meaning that XYZ is merely leasing “unlit” fiber optic cable – otherwise known as “dark fiber”. Hence, in order to activate the fiber optics the leasing entity must energize or “light” the fiber optics with an external electronic energy source. Alternatively, XYZ may also provide the energy source needed to “light” the fiber optic cable in which case it would be selling “lit fiber”. Keep in mind that only “lit fiber” can be used to transmit voice or data communications.

QUESTIONS:

1. Is the monthly leasing charge billed by XYZ Company to its corporate clients for the use of its unlit fiber optic cable (i.e., “dark fiber network) subject to the Utah State Sales Tax?

2. If so, what is the theory upon which taxability is based?

For example, do charges for dark fiber leasing fall within the scope of either a lease of tangible personal property or a lease of real property or does some other theory of taxability apply? (Please specify exactly how dark fiber leasing agreements are classified.)

3. If charges for the leasing of dark fiber are treated as a taxable lease of real property or tangible personal property, please identify the section of your state’s statutory code, which supports such a basis of taxability.

4. Finally, are charges for the use of “lit fiber” subject to taxability as a form of pure telecommunications service? (Please explain the concise reason for such a determination.)

You may reply in writing via return letter or if you prefer you may fax your reply to our office at FAX #####. Thank you in advance for your prompt and courteous written response to our taxability query.

Sincerely,

NAME
COMPANY

RESPONSE LETTER 07-009

April 4, 2008

NAME
COMPANY

Re: Private Letter Ruling Request 07-009
Treatment of the Lease and/or Use of Unlit and Lit Fiber Optic Cable

Dear NAME:

We have received your letter requesting a ruling regarding the tax treatment of certain transactions relating to the lease and/or use of unlit or “dark fiber” optic cable and the use of lit optic cable. You represented that COMPANY, a DIVISION, hereinafter “COMPANY, develops tax compliance software that you market to various telecommunications providers. COMPANY would like to include the tax treatment of these transactions in its database. You also provided an illustrative fact pattern to assist us in making our determination as to the tax treatment of the “dark fiber” and lit optic cable. Our ruling is based on the following fact pattern, and could differ if the facts are changed from the following scenario. We must assume that your example is hypothetical so we can make no commitment that our ruling will apply to any specific company.

Fact Pattern: XYZ Company is a Local Exchange Carrier licensed to do business in Utah. XYZ owns a network of fiber optic cable which, when activated, is used to support voice, data, and internet service applications. These cables are buried underground and accessed through highly secured locked-box locations.

You have asked three questions concerning the taxability of the “dark fiber” product: 1) whether the monthly leasing charges for the use the dark fiber network is subject to Utah State Sales Tax; 2), if monthly leasing charges are indeed subject to Utah State Sales Tax, under what theory are they taxable; and 3) if leasing charges are treated as taxable leases of either real property or tangible personal property, under which Utah code is this determined. You also asked one question concerning the taxability of “lit fiber”: whether charges for the use of “lit fiber” is subject to Utah State Taxes as a form of pure telecommunications service. These questions will be addressed below.

Generally, taxation of telecommunications service is governed under Utah Code Ann. §59-12-103 which imposes tax on the purchaser for the following types of transactions:

(1)(b)(i)(A): amounts **paid to a telephone service provider** regardless of whether the telephone service provider is municipally or privately owned

...

(1)(k): amounts paid or charged for **leases or rentals of tangible personal property** if within this state the tangible personal property is: (i) stored; (ii) used; or (iii) otherwise consumed

Id. (Emphasis added.)

To address the potential tax implications associated with the lease and or use of either lit or unlit fiber optic cable, the following definitions are necessary. A telephone service provider is defined in UCA §59-12-102(105)(a) as:

“a person that: (i) owns, controls, operates, or manages a telephone service; and (ii) engages in an activity described in Subsection (105)(a)(i) for the shared use with or resale to any person of the telephone service.”

(103)(a) telephone service is “a two-way transmission: (i) by: (A) wire; (B) radio; (C) lightwave; or (D) other electromagnetic means; and (ii) of one or more of the following: (A) a sign; (B) a signal; (C) writing; (D) an image; (E) sound; (F) a message; (G) data; or (H) other information of any nature”

Id.

Dark (or Unlit) Fiber Optic Cable:

In your scenario, the fiber optic cable is not activated or lit, and the customer must supply its own energy source to activate (or light) the fiber. XYZ, the owner of the network of fiber optic cables, is merely leasing the right to use its cables.

Only leases or rentals of tangible personal property are taxable. The taxability of utility lines is outlined in Tax Commission Publication 42 as “... generally considered real property if installed underground or permanently attached over ground.” (Id. at 1.) As described, the cable is a utility cable installed underground, therefore these transactions involving the leases of “dark fiber” (unlit fiber optic cable) are treated as a lease of the use of real property. Under UCA §59-12-103, this type of use or lease of real property is not subject to Utah sales and use tax.

Lit or Activated Fiber Optic Cable:

In your scenario, XYZ, the owner of the network of fiber optic cables is providing the energy source to activate the cables. The lit cable is used to transmit signals within the above statute as telephone service and thus XYZ, the owner of the network of fiber optic cable should collect tax on these transactions as a telephone service provider. Telephone service is subject to Utah sales and use tax under UCA § 59-12-103(1)(b). In this transaction, XYZ meets the definition of a “telephone service provider” pursuant to UCA § 59-12-102(105)(a) and is providing “telephone service” as defined in UCA § 59-12-102(103).

Lastly, as a telephone service provider, XYZ must collect taxes relating to the establishment of 911 emergency telephone service; a Poison Control Center; and a unified E-911 emergency service as authorized under UCA §§ 69-2-5, 69-2-5.5, and 69-2-5.6, respectively.

This conclusion is based on the information provided to us in your fact pattern. As previously stated, our responses could be different if the facts are other than those in the above fact pattern. Should you have further questions, please contact us.

For the Commission

Marc B. Johnson
Commissioner

MBJ/cms